SPECIAL ~~1990~~ ISSUE

FORTUNE

1990 INVESTOR'S GUIDE

WHERE TO PUT YOUR MONEY FOR GROWTH AND SAFETY NOW

Building wealth for your retirement, PAGE 28

Five pros show how to allocate assets, PAGE 125

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Also: gold, real estate, and much more . . .

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FALL 1989

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"The biggest risk at 65 is to put your money to sleep. You have the problem of your purchasing power being eroded by inflation. Call it the Aunt Tilly effect."

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COVER: The photographs were taken by Rita Maas.

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"You don't need a rocket scientist. Investing is not a game where the guy with the 160 IQ beats the guy with the 130 IQ. Rationality is essential."

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"Dying ain't nothing compared to figuring out the tax code. Dying in the next ten years would be real bad tax planning."

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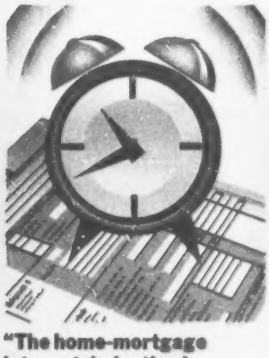

"The home-mortgage interest deduction is going to go. Now that the lawmakers have established the principle, they can chip away."

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"I started in this business during the bear market. My motto is 'It isn't how fast you run up the mountain. It's making sure you don't fall even once.' "

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EDITOR'S DESK

That giddily surging stock market of early October made many investors both eager and anxious. Should they buy? Sell? Or just pray that October 1987 wasn't about to happen all over again? Our fifth annual Investor's Guide provides a treasury of answers—and the timing couldn't be better. This special issue also reminds us of some fundamental principles, notably that in a volatile economic environment, allocating your assets with an eye on the *long term* is the only sensible approach.

Keith Johnson, a member of FORTUNE's board of editors, assembled and directed a crew of more than 40 for this year's Investor's Guide. Says Johnson, who has been in charge of each of the five Guides: "If you look to the long term, you're almost certain to come out ahead. And you should be able to hear the news that the Dow has dropped 500 points and—if not laugh—at least not cry."

Two principal members of Johnson's team are Edmund Faltermayer, who has edited FORTUNE's Personal Investing column for seven years, and John Curran, our senior investment writer. Faltermayer served as editor of Curran's quarterly report on investment strategies, among other stories. Curran was the author of three of the four articles identifying strategies for today's markets and edited three other stories on building assets for retirement, paying for college tuition, and making the most of a company savings plan. He bought his first share of stock at age 12 and has been writing about the markets since 1976. He's a firm believer in consistency and in waiting for the right opportunities to come along. "We're trying to teach people not to go for the big kill," he says. "Stocks are not as risky as some people believe, and they are more rewarding than some people believe. But you need to think long range."

This year's Guide also investigates a broader variety of investments than before, from writer Brett Fromson's story on opportunities overseas, "The Smart Way to Go Global," to reporter Alan Deutschman's article, "How to Invest in a Startup Business," which may help you fend off anybody who wants you to help finance a diner serving Rumanian-Thai cuisine.

Bringing visual elegance and continuity to such a breadth of material was the challenging task of designers Frances Fifield and Jim McManus. "It's difficult and demanding to create a look that works in so many different situations," says Fifield. But we think she has—and that you will find the Guide attractive, timely, and useful.

Marshall Loeb
MANAGING EDITOR

NINA BARNETT

Johnson (foreground) with key members of the special issue staff

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MANAGING YOUR COMPANY PLAN

Whether you're a loyal company man or a career grasshopper, you can do plenty of things to get more bang from your company savings plan. First among them: Understand the types of plans you are dealing with. They come in several varieties, and they differ in important ways—such as who makes the contributions, how they are taxed, and how much money can go into them each year.

The most popular are defined-contribution plans, where you put money in tax-free and it compounds tax-free until you withdraw it. These include Keogh plans for the self-employed and employees of unincorporated businesses, and 401(k) plans for employees of for-profit corporations. In 401(k) plans, both you and your employer may make contributions. Your own annual contribution may not exceed an amount indexed to the cost of living; in 1989 that ceiling was $7,627.

Your job is to integrate your 401(k) assets with your overall long-term investment strategy. As a tax-sheltered account, your 401(k) is an ideal nest for investments that throw off a lot of taxable income—bond funds, high-dividend stock funds, and stock funds that make frequent capital gains distributions.

The choices you're offered for investing your 401(k) money are limited, but one of them is usually a diversified stock portfolio, often managed by a mutual fund company. Unless you are already heavily invested in stocks outside of your 401(k), this is probably your best bet.

In many company plans, investors put too many of their eggs in a single basket—their company's stock. If your company is contributing stock to your 401(k), for instance, don't steer a big percentage of your own contributions into its stock as well. After all, your job is your most valuable asset. If your company goes out of business, a heavy commitment to its shares will compound the blow to your finances. The problem is especially acute when a big percentage of the plan's assets are tied up in an employee stock ownership plan. ESOPs give long-term employees a chance to sell some of their company shares when they near retirement. If you're offered that opportunity, seize it.

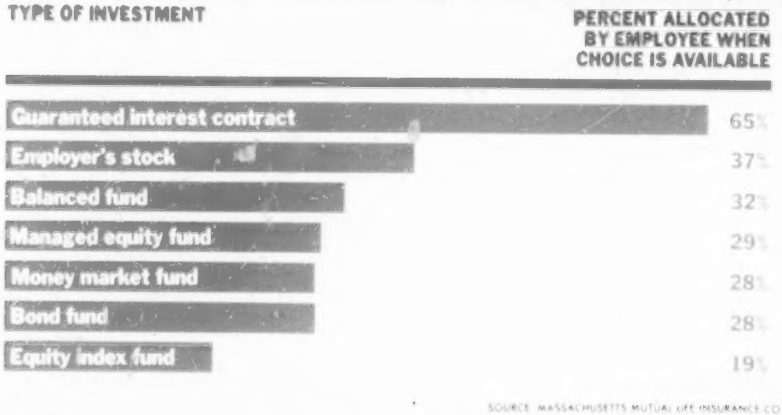
The most popular choice among 401(k) participants is a guaranteed interest contract, or GIC. Unfortunately, it's also among the least desirable for long-term investors. These contracts, offered by life insurance companies, guarantee a stated rate of interest for the life of the contract, typically one to five years. In the hotly competitive market for retirement fund money, GICs have been yielding up to 8.5% on one-year contracts and 9% on five-year deals. But as with bank CDs, which they resemble, yields drop when interest rates decline.

The GICs' resemblance to CDs also extends to preserving your principal. The value of your investment does not change to reflect shifts in interest rates. Unlike CDs, however, GICs are not backed by any form of federal insurance. They are only as sound as the company issuing them. The biggest problem with GICs is that over the long run their performance roughly tracks that of five-year Treasury bonds. If that sounds appealing, consider that since 1926 those intermediate Treasuries have provided an annual average return of only 4.8%.

When you leave the company, you have a window of opportunity for reallocating your 401(k) money. If you don't like the investment options the company plan offers, transfer your funds into an IRA. With an IRA, your investment horizon expands to include the whole world of securities and mutual funds. A self-directed IRA in a Charles Schwab account or in Unified Management's Unisave account, for example, gives you a crack not only at discount brokerage services but also at investing in a wide range of load and no-load funds.

When you finally retire, 401(k)s give you one tax advantage that IRAs don't. With a 401(k) you can take out all your money at once and cut your tax a bit by using the five-year forward-averaging method. That's great if you expect to use the money not for income but to buy a boat or a cottage by the sea.

HOW WORKERS INVEST 401(K) FUNDS



SOURCE: MASSACHUSETTS MUTUAL LIFE INSURANCE CO.

Despite lackluster returns, guaranteed interest contracts are the most popular place for employees to put 401(k) money. They far outdraw more rewarding equity funds.

complex. Warns Jere McGaffey: 'You must make sure you have absolutely no equity or interest left in the business at the time of your death or else the entire value of the company may revert to your taxable estate." Thus, you must be able to predict with some accuracy when you are going to die.

Although 2036(c) is couched in such fuzzy and all-encompassing language that tax lawyers have yet to work out its full implications, a few brave souls are attempting to get around it. One of them is Jack Babbitt, the founder and owner of Devco, a chemicals company based in Tulsa with a complicated constellation of interests in petrochemical companies situated in California, Canada, Saudi Arabia, and Chile. Babbitt, who was married for 39 years, widowed, and remarried, has three children in Tucson, Arizona; Los Angeles; and Mid-

DAVID STOCK—ONYX

Ron and Carol Moceri's "remarriage insurance" cuts out the survivor's spouse.

land, Texas. His goal is to pass equal ownership of Calsulco, an 80%-owned subsidiary of Devco, to his son, who is now running it, his two daughters, and their respective spouses.

Babbitt sought the advice of Charles Rains, an attorney at Sutin Thayer & Browne in Albuquerque, New Mexico, who specializes in brain twisters like this one. Rains has stitched a crazy quilt of trusts, gifts, and guesswork. First, the Helen Babbitt family trust, created by Babbitt's first wife with Babbitt and his kids as beneficiaries, bought 40% of Calsulco's closely held stock. Next, a 40% chunk of the company's tangible assets went into a GRIT, with the new maximum allowable term of ten years. Third, Babbitt and his wife are giving a total of $120,000 worth of Calsulco's common stock to the three children and their spouses each year for the next five years—the maximum the couple can give without incurring gift taxes. "By using a GRIT we've in essence tied Jack to the ten-year term," notes Rains. "If he dies before the trust expires, everything goes back into his taxable estate." Or as Babbitt puts it, "Dying in the next ten years would be real bad tax planning."

No matter how many trusts you have, and however ingenious their construction, you still need a will. Assets you use all the time—checking accounts, cars, jewelry, and other day-to-day pleasures and necessities—aren't trustworthy, so to speak, but they are still worth passing on. A will attests to your intention that someone after you should enjoy, enjoy. Ernest Milani, 60, took this notion to heart. He is the Northeast president of CDI Corp., an engineering and technical services company headquartered in Philadelphia, and his will is 80-odd pages long.

In it Milani has spelled out the disposition of the family antiques and jewelry to help prevent squabbles among his three grown daughters and one son. And then there is the wine. His cellar has more than 3,000 bottles, willed to various oenophile friends. "I'm trying to drink it all before I go," he jokes, "but I may not make it."

Milani's estate plan has another unusual feature: a memorial trust from which the income will buy a round of drinks for the house at his favorite tavern every year on his birthday. "It started as a lark," he says, "but then it turned serious." His will covers a number of contingencies, such as what happens if the bar goes out of business (the free toasts will be raised in another location), and even provides for the bartender's tips. This liquid memorial should last about a century after Milani's death. Says Alexander Bove, the Boston attorney who helped him draw up his will: "By that time people will probably have forgotten who Ernie was, but they'll no doubt gladly toast him anyway." Even if you can't take it with you, you can arrange to leave 'em laughing when you go. F

THE STATES AND YOUR ESTATE PLAN

The rules that govern death duties in the 50 states were not created equal. If you move often or have assets in more than one state, you should know that not all states define property ownership the same way. Nine of them—Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin—have community property laws, which assume that you and your spouse both own all assets acquired during your marriage. But in common-law states, the person whose name is on the deed—or the bankbook, or the car title—is usually presumed to be the sole owner.

Say you live in Washington, a community property state, and own a vacation home there in your name only. Move to Oregon, a common-law state, and your spouse could lose any claim to the Washington house upon your death. One solution: Establish a joint tenancy with right of survivorship, which guarantees your spouse's share no matter where your estate is probated.

There's more. Suppose you summer in Greenwich and winter in Boca Raton, you lucky devil. As the table shows, Florida is far cheaper to die in than Connecticut, but for your heirs to profit from that fact you must legally reside there. First, a pleasurable duty: Spend as much time in Florida as possible. Then register to vote, register your cars, and keep your bank accounts there. Make sure your Florida address appears on your passport and other papers. To allay all doubt, attach to your will a sworn affidavit of your intent as to domicile.

Variations in state law can affect crucial details of your estate plan. On moving from Massachusetts to New York, BT Securities vice president Ira Weinman discovered that he could not serve as sole trustee of his revocable trust. Had he not named a co-trustee (he chose his brother-in-law) a New York judge could someday have declared his well-laid trust null and void. Most often, a move from one state to another doesn't require an earthshaking change in your estate plan. But check to be sure.

WHAT'S LEFT OF A MILLION DOLLARS, STATE BY STATE

The chart shows how big a bite taxes take from a $1 million estate left by a widow or widower entirely to a son or daughter. The feds tax anything over $600,000 at rates ranging from 37% up to 55%. In 31 states, the heir ends up with $847,000 after state and federal death duties. All 50 states impose what's called a pickup tax, which reduces the amount that goes to the U.S. Treasury because it is credited against the federal estate tax due. In addition, several states make heirs who are residents pay an inheritance tax on their legacies. The states with the st[illegible]est levies: Massachusetts, sure, but *Idaho*?

STATE	FEDERAL TAX	STATE TAX	AMOUNT LEFT FROM $1 MILLION
MOST STATES*	$119,800	$33,200	$847,000
VIRGINIA	$119,800	$34,196	$846,004
NORTH CAROLINA	$119,800	$35,000	$845,200
KANSAS	$119,800	$41,750	$838,450
OKLAHOMA	$119,800	$45,725	$834,475
RHODE ISLAND	$119,800	$50,040	$830,160
INDIANA	$119,800	$51,900	$828,300
NEW YORK	$119,800	$53,500	$826,700
DELAWARE	$119,800	$53,750	$826,450
CONNECTICUT	$119,800	$54,500	$825,700
OHIO	$119,800	$58,100	$822,100
PENNSYLVANIA	$119,800	$59,880	$820,320
WISCONSIN	$119,800	$61,125	$819,075
SOUTH CAROLINA	$119,800	$67,400	$812,800
SOUTH DAKOTA	$119,800	$69,000	$811,200
MICHIGAN	$119,800	$71,099	$809,101
IOWA	$119,800	$71,825	$808,375
KENTUCKY	$119,800	$84,950	$795,250
MASSACHUSETTS	$119,800	$105,500	$774,700
IDAHO	$119,800	$113,000	$767,200

*Alabama, Alaska, Arizona, Arkansas, California, Colorado, Florida, Georgia, Hawaii, Illinois, Louisiana, Maine, Maryland, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, North Dakota, Oregon, Tennessee, Texas, Utah, Vermont, Washington, West Virginia, and Wyoming.

SOURCES: ARTHUR ANDERSEN & CO.; ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS